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THE QUARTERLY

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VOLUME 6 NUMBER 1

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CONTENTS

Firm policies and procedures on technical matters are stated in our technical manuals, bulletins and letters. The opinions expressed herein on technical subjects represent those of the authors and are not to be construed as setting forth new or amending present firm policies and procedures.

E. PALMER TANG
Minneapolis

E. PALMER TANG graduated from the University of Minnesota in 1938 and was named the person who had contributed most to the School of Business Administration in that year.

He began work with the Minneapolis Office the same year and has been with the firm continuously except for three years in the army, including one year as a finance officer in Japan.

At the present time Mr. Tang is president of the Minneapolis Chapter of the National Association of Accountants and first vice president of the Minnesota Society of Certified Public Accountants.

THE OPEN DOOR

WE ALL HAVE ABILITIES which, at best, we never fully utilize. As the parable of the talents relates, one person buried his talent and accomplished nothing, while the other two used theirs which grew accordingly.

Our firm has always had men of ability, men of potential, men who can grow. But what transforms a latent ability to useful action? Let's take a few examples. What drives one individual to secure reference material and other useful data to prepare himself for an unfamiliar assignment; to devise a better accounting system which can be invaluable to a client; to spend the "five minutes more" required to uncover a defalcation? What motivates him to pursue a slim lead and perhaps secure a new client or a new engagement from an existing client, what makes him constantly tax-conscious and alert to suggest needed estate planning for family security? Why does he recommend more effective internal controls — thus saving a trusted employee from temptation — or convey a personal touch by seeking opportunities to discuss problems with management, or help an assistant over a rough spot and help him grow in the profession?

Can it be called ingenuity, inquisitiveness, conscientiousness, perseverance, understanding, helpfulness — or is it a desire to excel so compelling that a person is willing to make the sacrifices necessary to extend himself a little farther?

For we as a firm must build on people, people with vision and imagination. Each of us has an untold responsibility — to ourselves, to our families, to our firm and associates, to our clients — to do the best we can, which is better than we may have thought possible. The door is open. A progressive man is never quite aware that a job cannot be done. He is too busy doing it.

E. Palmer Tang

SIM

TRB&S HAS RECENTLY COMPLETED an extensive research and development project to explore the feasibility and desirability of using Operations Research techniques in the area of inventory management for a retail department store. Although this project was under the direction of the Management Sciences Division of the firm, much of the development work was done by members of the Audit and Management Services staffs of the Detroit and St. Louis Offices. Several man-years of effort were devoted to this project before a practical and economical inventory management system was designed. This system was given the name "Selective Inventory Management."

Operations Research

Before discussing some of the basic principles of Selective Inventory Management, we should consider the reasons why our research effort was directed to the retail industry. During the years following World War II considerable interest developed in the study of the feasibility of applying Operations Research (abbreviated OR) techniques to the solving of business problems. Most of the research efforts during these years were directed toward industrial situations. As our firm developed a staff of scientists qualified in OR techniques, we decided to explore the areas in retailing wherein OR techniques might have application.

Our preliminary research in retailing was motivated by the fact

SELECTIVE INVENTORY MANAGEMENT

by Jack K. Wirth and Nicholas J. Radell

that little had been accomplished in retailing in this area, and by our belief that the field of retailing presented an excellent opportunity for the application of OR techniques. We also felt that, because of our firm's dominant position in the field of retailing, we had an obligation as a firm to lead in the development of some new ideas and useful techniques which would represent a significant contribution to the management of retail enterprises.

The early research in the application of OR techniques in retailing suggested several problem areas which might benefit from a scientific approach. The determination of the size and location of warehouses or branch stores were problems suited to the use of mathematical techniques. Other questions of importance to management such as the effect on sales of night openings or promotional advertising were also suitable for the application of OR techniques. However, our preliminary research indicated that the area in which a significant impact could be made quickly was inventory management.

Inventory management is one of the most pressing problems facing retailers today. In the day-to-day operation of any store, a large number of inventory buying decisions must be made. With the growth in size of main stores and the addition of branch stores, the number of buying decisions have been multiplied to the point where buyers are finding it difficult to handle effectively the routine buying decisions and still devote the necessary time to other merchandising problems such as promotions and the selection of new items. As a result, many of these buying decisions are being made hurriedly based upon piecemeal information or are being relegated to untrained clerical personnel.

Upon considering this problem, it became apparent that the development of "decision rules" to assist a buyer in making inventory management decisions would represent a significant aid to the effective management of inventory. Operations Research and its associated mathematical inventory theory could furnish these decision rules.

This mathematical inventory theory is particularly applicable to staple, nonfashion merchandise which has a stable sales pattern and is frequently reordered. In typical department stores, it is estimated that the merchandise in from 25% to 50% of the departments would fall within this classification. These high reorder departments include such departments as housewares, hardware, drugs, notions, men's shirts, cosmetics, and others.

Taking all of these factors into consideration, the decision was made to direct our research on the application of OR techniques in retailing to the problem of inventory management.

Inventory Management System

Our objective was to design a system which could be utilized by a retail store in the management of departmental inventory without incurring significant additional cost for its installation or operation. The system had to be practical and one that could be operated by clerks with a minimum of supervision. The design of the system was, therefore, purposely made simple and unsophisticated.

The nature of retail merchandising imposed some other limitations on the system design. The system had to be compatible with existing monetary inventory controls and also be acceptable to the buyers and merchandise managers who would have to work within the requirements of the system.

With these factors in mind, we proceeded to design a scientific inventory management system which we called Selective Inventory Management, which in turn was referred to as SIM. Since its original conception, the basic principles of the system have received considerable publicity both within the firm and in retailing circles generally. The Management Sciences Division of the firm has issued a technical report on the system which should be referred to for a more comprehensive discussion of some of the basic concepts of the system.

The purpose of this article is to set forth in nontechnical terms some of the background and basic concepts of SIM. From this we hope that members of the audit staff particularly will better understand what SIM is and what it can accomplish in the area of inventory management. As will become apparent from this article, while SIM was designed to be used in the management of inventory in a retail department store, the principles of the system design are readily adaptable to industrial situations. For example, with some modification SIM could be used effectively for the management of inventory by an automotive parts supplier, a distributor of surgical instruments, or any enterprise where the inventory is characterized by a large number of items which must be frequently reordered.

Design Considerations

SIM uses two rudimentary scientific inventory formulas for determining "when" and "how much" of a given item to reorder. The mathematics used in SIM are neither complicated nor new to the theory of inventory management. The classical economic lot formula used in SIM has been known for years. However, the number of applications in retailing activities have been limited. There were two major reasons for this. First, when retailers attempted to apply mathematical inventory theory, they usually found that the installation and operating cost of the associated inventory system was prohibitive. Second, many retailers felt that it was too difficult to accurately forecast retail sales. Consequently, any formula which required the use of forecast sales would be inaccurate and could not yield better inventory decision information than a "rule of thumb" decision based upon a buyer's intuition or experience.

Preliminary investigation indicated that the first reason was a more fundamental objection than the second. Relatively simple forecasting rules have been used with acceptable accuracy in departments where the theory seemed most applicable. Therefore, the problem of developing a practical system using known mathematical inventory concepts appeared to be the principal obstruction in the application of the theory.

An inventory management system had to be designed which would provide the discipline of consistent decision rules applied on an item-by-item basis and yet which could be administered and operated by existing department store personnel with a negligible increase in operating costs. At the same time, the associated installation costs had to be small enough to assure their recovery in a relatively short period of time.

Selectivity

The major contribution of SIM to the theory of inventory management, and the underlying concept which makes SIM a practical system for the retail industry, is the reallocation of available management and control effort to each of the inventory items in proportion to their contribution to total sales of a department. By applying the concept of selectivity, effective management and control are obtained without prohibitive cost of operation.

In the departments studied, each item in the inventory tended to receive approximately the same amount of control effort under the existing systems. The departments studied carried from 2,400 to 6,000 items. Under SIM, control effort was redistributed so that those items which made the greatest sales contribution to the department were most carefully controlled.

To determine the items which made the greatest sales contribution to the department, the inventory was classified by annual dollar sales. This classificaion indicated that the items in the department's inventory would fall roughly into three groups, as follows:

CLASS	PER CENT OF ITEMS IN INVENTORY	ESTIMATED PER CENT OF TOTAL YEARLY SALES
A	10%	50%
B	40	40
C	50	10

This pattern of selectivity repeated itself in every department studied. Utilizing this information, we were able to classify the inventory into three groups which we identified as Classes A, B, and C. We then suggested a reallocation of available management and control effort so that the items in Class A would receive the largest amount of effort per item and Classes B and C items would receive correspondingly less effort. Some of the areas in which a reallocation of management and control effort was made, for example, were:

1. The forecasting of yearly sales and lead times
2. The review and updating of these forecasts
3. Stock counting
4. The setting of buffer or safety stocks

Mathematics

Having established the concept of selectivity and the associated reallocation of management and control effort, it became feasible to apply the mathematical formulas to compute optimum reorder quantities (how much to buy) and to determine the statistical reorder points (when to buy).

The formulas used for determining reorder quantities and reorder points are an essential element of SIM. The principal value of the formulas in the system is that they provide a basis for making consistent inventory management decisions for each item to which they are applied.

There is nothing complicated about the formulas used in SIM. They can be easily understood by anyone who is not bothered by the use of symbols rather than words to express a relationship of factors. For an understanding of SIM, it is not necessary to understand the mathematical derivation of the formulas or even to be able to perform the calculations necessary to solve the equations. Our technical staff has developed simple tables which can be used by the clients' clerical personnel for determining reorder quantities and reorder points.

Optimum Reorder Quantity

The optimum reorder quantity (Q) is the quantity of an item which is ordered each time the reorder point (P) is reached.

The formula used to determine the reorder quantity (Q) is:

$$Q = \sqrt{\frac{2 \cdot C_1 \cdot S}{C_2 \cdot i}}$$

Where

Q = economic reorder quantity (in units)
S = annual demand (in units)
C_1 = cost of placing an order (in dollars)
C_2 = unit cost of the item (in dollars)
i = cost of holding inventory (as a % of unit cost)

This is one of the simplest of the optimum (most economic) lot-size formulas. More comprehensive relationships have been developed which recognize additional factors such as the cost of being out-of-stock.

A considerable amount of research effort was devoted to the study of the cost of ordering and holding inventory (C_1 and i). While the elements of cost which made up these factors could be defined with some degree of exactness, it was not possible to measure many of these costs with more than a general approximation. However, the useful application of the reorder quantity equation is not dependent upon a more accurate measurement of these costs.

Many past attempts to use the economic lot-size formula in the management of inventory never got beyond the frustrating study of determining finite values for these cost factors. The cost factors must certainly, to some extent, be imputed rather than determined by analysis. A successful if not theoretically ideal application of the formula can be achieved by employing imputed cost factors.

Statistical Reorder Point

The other formula used in SIM to determine the statistical reorder point (P) is:

$$P = B + \overline{m}$$

Where

P = reorder point (in units)
B = buffer or safety stock (in units)
$\overline{m}$ = average demand during the replenishment period (in units)

This formula says that the reorder point (P) is equal to ($\overline{m}$) the estimated sales of the item over the period of time required to get delivery of the item from the supplier plus (B) a buffer or safety stock. When the number of items remaining in stock and on order is equal to or less than the reorder point (P), the reorder quantity (Q) should be ordered.

Since $\overline{m}$ is an estimate based upon average sales rates per day and average lead time in days, it is expected that the sales rate or lead time, or both, would fluctuate above the average at least half the time. This would cause an out condition to develop unless a buffer or safety stock is provided. By assuming that the average demand will fluctuate in accordance with a known statistical distribution such as the Poisson* distribution, we are able to determine the buffer stock necessary to protect against fluctuations. A probability of going out-of-stock can also be associated with the size of the buffer stock. Since the

**The Poisson distribution is a mathematical distribution function which is commonly used for measuring the probability of events which have a small probability of occurrence.*

buffer stock is determined based upon a statistical distribution and associated probability, the reorder point is referred to as a statistical reorder point.

To approach a 100% probability that an order will be delivered before the stock of an item is exhausted would require a prohibitively large buffer stock. However, the retailer is able to specify a 95% or even 98% probability requirement and accordingly determine a buffer stock which will produce the desired result.

Again we would like to point out that the formulas discussed above are the classic inventory management formulas. They demonstrate the basic principles of the system. More sophisticated formulas have been developed and are being used in SIM installations.

Evaluation

Once the system had been designed, it was necessary to prove its value to retailers. To do this, the system was evaluated in terms of what the average inventory investment, number of days out-of-stock, and number of orders written would have been in the departments studied if the proposed system had been used during the year prior to our study. The Operations Research technique of "System Simulation" was used in this evaluation which was carried out using a randomly selected sample of items from each department studied.

For each of the items in the sample, historical stock data were obtained and plotted to show the item's inventory history during the test period. Average inventory investment, number of days out-of-stock, and number of orders placed were determined for each item. Totals for each of these factors were obtained for all items in the sample.

After the actual inventory histories were plotted, a simulated history was determined for each of the items based upon the reorder quantities and reorder points established by the formulas but using actual lead times and sales rates. Average inventory investment, number of days out-of-stock, and number of orders placed were determined for each simulated history. Totals of each of these factors were obtained for all simulated histories and compared with the actual histories.

The results of the evaluation showed a reduction in all three factors from the use of the proposed system. Days out-of-stock were reduced by 66 per cent in one of the departments studied and by 20 per cent in the other department. At the same time, average inventory investment was reduced by 22 per cent in the first case and by 31 per cent in the other. Number of orders written was reduced slightly in each instance.

Through the system simulation, we were able to demonstrate to the retailer that by using an inventory management system which utilized mathematical formulas, within a system design based upon the concept of selectivity, he would be able to achieve reductions of both average inventory and number of days out-of-stock. Furthermore, he would be able to do this with an inventory system designed to be operated by his present personnel.

Several of the retailers were somewhat skeptical that the proposed system could achieve a reduction of both average inventory and number of days out-of-stock. In order to understand how the use of mathematical formulas made this improvement possible, it is necessary to understand how changes in inventory affect days out-of-stock. As average inventory increases, the expected number of days out-of-stock will decrease, *but not in direct proportion*. The converse is true for a decrease in average inventory. As a result, the mathematical formulas will reduce inventories of items which were overstocked and increase inventories of items which were critically understocked. Because of this nonlinear (not in direct proportion) relation between average inventory and days out-of-stock for each item, the net result can be a decrease in both inventory investment and days out-of-stock for the aggregate inventory.

Other Benefits

It is also important to recognize that by the use of the formulas it is possible for management to trade off inventory investment against stock-outs. The retailer may specify the desired in-stock condition for a department and the system will provide the minimum level of inventory investment and the fewest number of orders written consistent with this decision.

In addition to the potential improvement in customer service brought about by a reduction in stock-outs and the cost savings realized from the reduction in inventory investment, there are many other benefits which are by-products of the system. The most apparent of these are the improvements in the administrative procedures of the department as they relate to inventory management. The establishment of a disciplined manual system for the management of inventory also provides a sound basis for the extension into the use of electronic data processing equipment. As another by-product of the system, buyers are furnished with more item information on which to base promotional decisions and decisions with respect to items to be added or dropped from the inventory.

What a client thinks of SIM

The following comments setting forth many of the benefits which are by-products of a SIM installation have been extracted verbatim from an internal memorandum prepared by the Divisional Merchandise Manager of the Housewares Division at one of our clients where an installation of SIM is being made in selected departments in the Housewares Division. The memorandum was addressed to the Merchandise Manager of the Home Division.

"The many unexpected and cost reducing benefits resulting from the as yet unfinished first year plan promise favorable budget reductions. Here, aside from the high 'in stock' position already achieved by Selective Inventory Management, is a list of the known benefits:

1. The Dennison stock control system is not needed in Paints, since the high 'in stock' position permits us to forward all send saleschecks to the warehouse without the need for attaching a Dennison sticker.
2. As an indication of the systems efficiency, we are pleased to report that the average number of daily unfillable warehouse sales tips is less than one per day per store.
3. While this is difficult to measure (we'll have actual figures after the completion of a full year) we have reduced paint transfers to each store, for further delivery to customers, by well over 20% compared to 1958.

   In other words, more deliveries are being effected through warehouse stocks, instead of store stocks, since all salesforces are now confident saleschecks will be filled promptly. This really results in a double saving — (1) eliminating many transfers to the stores and (2) returning sends to the delivery stations.
4. Mr. ____, the Assistant Buyer, estimates that SIM reduced the time he gives to reordering merchandise by two hours a day, freeing him for other supervisory work.
5. Mr. ____ further reports an intangible but still considerable clerical time saving in order writing. This amounts to approximately an

hour per day. In addition, another hour per day is saved by eliminating the posting of receipts in branch store books.

6. Since orders are written based on warehouse stock only, orders can be written the same day as the count is taken and confirmed the following day, whereas in the past it took some time to get stock counts from all locations before orders could be written.
7. Everyone concerned also agrees that counting of inventories is not only more efficient and accurate (something rarely achieved under other systems) but this too reduces costs through time saved. Considerable time is saved for improved customer service and more effective selling, because demonstrators no longer maintain their own stock books, go to the warehouse to take stock counts, and fill their own requisitions at the warehouse as they customarily did. This savings amounts to approximately four hours daily.
8. Perhaps most important of all is the excellent morale of our salespeople. They now know that stocks are in good condition, and that promises of delivery to customers can be confidently made and fulfilled.

Jack K. Wirth
Detroit

After receiving his MBA from the University of Michigan and spending three years in the Air Force, Jack Wirth joined TRB&S in 1954. On February 29, Mr. Wirth left to accept a position with the Continental Aviation and Engineering Corporation.

Nicholas J. Radell
Management Sciences

Both a CPA and a registered Professional Engineer is Nick Radell, a graduate of the University of Michigan. In his work he has been concerned mostly with the application of Operations Research techniques to the retail industry.

9. The requisition-count sheet form, replacing the branch stock books and the inter-store requisition, designed for the SIM system is so efficient and carries so much more information than the inter-store transfer, that every buyer in this division wishes to adopt this form. Unfortunately, this is not possible for wide acceptance since the warehouse sequence stocking of reserves is not coordinated with the item listing on the requisition-count sheet requisition."

Development effort is being continued to further refine SIM and add more sophisticated OR techniques to its design. In addition, consideration is being given to the eventual adaptation of the system to electronic data processing equipment.

Members of our Audit and Management Services staffs are encouraged to become familiar with the basic principles of SIM and what it can offer our clients in retailing and in other areas. We can perform a real service for our clients by making them aware of this improved system for the management of their inventories.

Executive Partners Meet in New York

Kenneth Mages points out needed change in executive office's new layout to Managing Partner John W. McEachren and Robert Beyer (both seated). Looking on are (from left) Wallace M. Jensen, Thomas J. Ennis and Donald J. Bevis.

Misapplied accounting idles two machines while others work overtime . . .

HOW "ALL-PURPOSE" DATA C

by Robert G. Stevens, Ph.D.

Detroit

LIKE MANY OF OUR CLIENTS, the XYZ Company re-evaluated its burden rates once each year. These burden rates were of the full-absorption variety and based on estimated volumes as opposed to practical capacity or normal volumes. Therefore, when volume estimates were low, burden rates were high. If the estimates went up, the rates would go down.

In their particular industry it was customary to issue bids or quotes on business, and their cost estimating department was charged with this responsibility. The cost of a particular item was established by analyzing blueprints to determine material requirements and to determine the manufacturing operations which would be required to fabricate the part. The estimated time required to perform each operation was determined by reference to engineering standards or historical data concerning past performance on similar products. Direct labor rates and the absorption burden rates for the various operations were supplied by the accounting department.

These cost estimates provided a basis for determining selling price and also became a basis for preparing shop orders. Then the sales department established the final selling price by adding a standard markup. Some orders would be reviewed by the sales executive and the standard markup might be adjusted to meet market conditions or the quotation might be referred back to cost estimating to explore the possibility of a more economical way to fabricate the product.

AUTHOR STEVENS received his B.S. degree from Southern Illinois University in 1951 and was a first lieutenant in the Air Force until 1953. He then entered the University of Illinois, earning his M.S. in 1954 and a Ph.D. in 1958. Mr. Stevens joined TRB&S later that year.

:EFEAT GOOD MANAGEMENT

Costs Seem to Rise for Two Machines . . .

In 1958 it was estimated that there would be relatively little demand for the quality of product which could be made on Press III, and only a small volume of work was anticipated which would be adaptable to the automatic saw operation. Since certain fixed costs were both directly related and allocated to these operations, the absorption burden rate was considerably higher than that in previous years and also higher than the 1958 rates for similar operations which were based on more "normal" volume forecasts.

When the first quotations involving these operations went through, the standard selling price was obviously not one that customers would pay. Investigation resulted in the sales department questioning the new burden rates for Press III and automatic sawing. But the discussions with Accounting only convinced them that the new burden rates did reflect the actual costs of these operations. Profits on individual jobs would also be determined and reported on the basis of these burden rates. They certainly did not want to sell anything below cost or to look bad on sales reports.

. . . So These Machines Stand Idle

The obvious answer was simply to avoid the use of these operations. The cost estimating department, therefore, assigned orders to hand saw instead of automatic saw. Presses I and II were used in preference to Press III. The manufacturing and production scheduling departments were also convinced that these were high cost operations. As was customary, they fabricated jobs in conformity with the operations indicated by the cost estimating work sheets. As a result, very little work was done on the automatic saws, the Press III area was used for storage space and, worst of all, overtime and night-shift premiums were paid to the crews of Presses I and II to keep up with the work load.

Contrary to what some might conclude, the management of the XYZ Company is exceptionally competent. Many companies make no effort at all to relate production scheduling to production costs.

This is a case in which good management was misguided by a poor application of accounting. The data used were acceptable for purposes of income determination but were not valid for this operating decision. Data developed under the concepts of Profitability Accounting, however, were valid. Under a new system of accounting, the cost estimating department is concerned only with the variable costs of manufacturing operation.

These variable costs provide a valid basis for determining the least-cost combination of operations required to fabricate a particular product. The absorption of fixed cost is considered a function of determining periodic income, and adjustments are made to arrive at balance sheet values for inventories which are consistent with generally accepted accounting principles. Fixed costs are also important in break-even analysis, and they are given proper consideration in cost control and in pricing.

The Need for Data Is So Great

It is safe to say that almost all accounting data in existence today are intended for the specific purpose of preparing balance sheets and income statements. These same data are probably being used for an infinite number of diverse purposes because there is such a great need for data. Accounting is a powerful force. Its apparent preciseness instills confidence, and very few who use accounting data are in a position to refute its validity. What happened to the management of the XYZ Company is probably happening to the management of many companies today.

Good Work for Pittsburgh Office Client

Misplaced decimal makes $42,000 overpayment

An overpayment of $41,749.56 was discovered by John C. Williams during an examination of a Pittsburgh client's financial statements. The overpayment related to the purchase of Federal Tax stamps to be affixed to the original issue of certain stock certificates. Mr. Williams noticed that the bank requested payment of $4,757.50 in connection with an issue of 275,000 shares of common stock, but had charged $46,388.40 for approximately the same number of shares in a similar issue. Analyzing this expense, Mr. Williams questioned the big difference between the two amounts and determined the correct figure to be $4,638.84—not $46,388.40. When notified, the bank acknowledged the error.

Plant accountant writes checks to himself

While working at a subsidiary of the same client, Theodore R. Miller found an irregularity in the imprest payroll bank account.

The plant accountant, Mr. X, wrote checks to himself for $500 during March and April without the knowledge or consent of the plant manager. The money was repaid to the payroll account in November and during the interim was shown as "wages paid in advance" on monthly bank reconciliations. The cancelled checks involved were withheld from the regular files by Mr. X.

Although the amount was nominal and was repaid before our audit, it did indicate a weakness in control over plant bank accounts which we had pointed out in our last letter of recommendations to this client. The needed control has now been instituted.

Baltimore Office Opens

Our newest office was opened January 1 in Baltimore at 10 Light Street. Karney Brasfield is the partner in charge of Baltimore as well as the Washington Office. John Rihtarchik is audit manager and will supervise audit staffs in both cities. Four other members of the Washington staff now assigned to Baltimore are Donald E. Hudson, Hugh V. Cochrane, David A. Forslind, and Thomas M. Fox. Marjorie Patterson is the secretary.

Why we have ta
and wh

The progressive features of the Federal individual income tax are well publicized. These of course affect partnerships and fiduciaries as well as individuals, since the income of all of these entities is eventually taxed at individual rates. The corporation income tax is also more progressive than is probably generally realized. The greater importance of the $25,000 surtax exemption to the smaller corporations, and other factors such as minimum accumulated earnings credits tend to make the impact of the corporate income tax much more severe on the corporations with larger earnings.

All of this emphasis on progressive rates means that tax problems really arise when one entity has a large amount of ordinary income. Lowering these progressive rates then becomes a matter of having more taxable entities, having the income taxed to the most advantageous entities, or using statutory advantages, such as tax exempt income, capital gain rates, etc. Before discussing in detail methods of paying tax at lower rates, however, we should consider the importance of deferring the payment of tax.

Deferral of Tax

The first preference of any taxpayer would be to pay no tax at all. The only legal way I know to accomplish this, however, is to have no

roblems—

do about them

by Durwood L. Alkire
Seattle

income, and this is not generally a satisfactory solution! It is probably not generally realized, however, that the indefinite deferral of the payment of tax is nearly as good as not paying the tax at all.

Perhaps you can see the importance of deferring the payment of tax, if you consider how desirable it would be to you personally if someone should offer you the use of $100,000 interest-free for an indefinite period. When you go on from this to considering the importance business, in general, places on working capital, the growth of sales and leasebacks and other methods to conserve cash, it becomes apparent that the indefinite deferral of a payment is extremely important. Some methods of deferral of tax available to most taxpayers are the use of fiscal years, the choice of depreciation methods, and the choice of methods of accounting, and we will consider these three methods now.

Use of fiscal years

Internal Revenue Service statistics show that about one-third of corporations filing income tax returns are now on a fiscal year rather than a calendar year basis. This percentage has been steadily increasing, since in recent years about three-fourths of the new corporations are adopting fiscal rather than calendar years. Actually, it has always seemed to me that there is no reason for more than one-twelfth of corporations being on the calendar year basis, with the exception of some types of corporations, such as those in regulated industries, that may be required to report on a December 31 basis.

Those flexible fiscal years

I realize that as certified public accountants, we can readily be accused of some bias on this question, as we must admit we are interested in filling out the "valleys" and pushing down the "peaks" in our own practice. Nevertheless, it still is generally in the interest of the client to be served by us at a less rushed time of year. We have had two gratifying experiences along this line recently in Seattle. The first was a partnership client considering incorporating, who asked us what fiscal year the corporation might adopt that would be most convenient for us; the second was a new corporation adopting an October 31 fiscal year, principally so that we could get our work done ahead of our busy season, and probably complete our work and give the client results for the year's operations in less time after the end of the client's year.

The tax advantage of a fiscal year from a deferment viewpoint will come principally in a seasonal business when a fiscal year can be selected that ends just before the peak income season. For example, we have an agricultural client on a May 31 fiscal year whose income is principally received during the summer months. The result is in general that expenses are deducted in one year and the income deferred to the next, so that there is a more or less permanent deferral of tax on one year's income.

In addition to the tax deferral possibility, fiscal years offer some flexibility in dealings with individual officer-stockholders of closely-held corporations, who are generally on a calendar year basis. There seem to be less problems in dealing with accrued salaries, interest on loans, etc. when the individuals and corporation are not all closing their years at the same time. A nontax benefit resulting from fiscal years is the elimination of extra work for employees at the holiday season, which generally comes with the use of a December 31 closing.

Choice of depreciation methods

There is considerable thinking that the accelerated methods of depreciation introduced by the Internal Revenue Code of 1954 are of no real benefit to taxpayers, as "you can only get your cost back once." This argument completely overlooks the value of deferring the payment of tax, the basic question we are discussing. In most companies, the use of these accelerated methods results in a more or less permanent deferral of tax. It is true that as to any individual asset or group of assets, larger depreciation deductions in the early years of the life of the asset will be offset by reduced deductions in the later years. In the normal situation, however, the reduced deductions in the later years of the lives of 1955 additions, for example, will be offset by increased deductions in the early depreciable years of the 1960 or 1965 additions.

The deferral of tax from the accelerated methods will generally end only with the liquidation of the company or the lack of additions to depreciable assets. This lack of additions is not likely with our present technical obsolescence, growth of business, inflation, and other factors.

When accelerated methods are inadvisable

We can conclude that the use of accelerated methods is generally advantageous, but there may be special situations where their use is inadvisable. These would generally be where a taxpayer was now paying low rates, could see the "end of the road" on its acquisition of assets, and hopes to have higher income, which of course means higher tax rates, later. For example, I discussed with an attorney his situation with a corporate client who was constructing a drive-in theatre. The capital asset acquisitions in the first year were quite substantial, but it was not expected that there would be substantial additions to fixed assets for some years to come. On the other hand, earnings were expected to be low or nonexistent in the early years, as in most new businesses, with the hope that they would grow as the business became established and attracted patronage. In this situation, the straight-line method would definitely be preferable to the usual declining balance or sum-of-the-years-digits methods.

This drive-in theatre might be a good place to use an "other consistent method" as allowed in section 167 (b) (4). Any consistent method is allowable if the total deductions in the first two-thirds of the useful life of the property do not exceed the total allowable under the declining balance method. Assume the theatre cost $60,000 and had a 30-year useful life. The total depreciation allowable under the declining balance method for the first 20 years would be approximately \$45,000. An "other consistent method" would be a modified, or two-step, straight-line method, with depreciation computed as follows:

$$\text{First 20 years} — \frac{\$45{,}000}{20} \text{ or } \$2{,}250 \text{ a year}$$

$$\text{Next 10 years} — \frac{\$15{,}000}{10} \text{ or } \$1{,}500 \text{ a year}$$

In general, the use of accelerated depreciation methods can be a tremendous help in building capital. Depreciation deductions have increased substantially in the last five years and now in effect furnish more funds by far than any other source, retained earnings, new securities issued, etc.

The additional first year depreciation of 20 per cent on assets acquired in any year up to a cost of \$10,000, introduced by the Technical Amendments Act of 1958, is of course a special statutory kind of acceleration. It is generally not too significant because of the \$10,000 limitation on the cost of assets, but may be interesting to a partnership with a large number of partners, as the \$10,000 limitation applies to each partner, and not to the partnership as a whole.

Choice of methods of accounting

The adoption of the most advantageous method of accounting furnishes another opportunity to defer tax indefinitely. For example, both the cash basis and the completed contract basis offer interesting possibilities along this line. By the use of the cash basis of accounting, a service organization may in effect use its accounts receivable as tax-free capital. A client of our Seattle office in a service business has remarked that it "seems illegal and *is* impossible" to build capital these days—but he goes on to say that his accounts receivable, on a cash basis, really represent his capital. These two methods of accounting, which may result in sharply fluctuating income, are particularly useful to corporations, as they have less of a problem with fluctuating tax rates than individuals who do not have steady incomes.

Any method of valuing inventory which results in lower valuations may result in an indefinite deferral in tax. The two principal possibilities are of course LIFO and cost or market, whichever is the lower. Cost or market, whichever is the lower, will of course only result in a lower valuation if there is some down turn in prices so that market becomes lower than cost. An interesting note on the cost or market, whichever lower method is the significance of indicating the election on the first return of a taxpayer. One author has recently suggested that a taxpayer might be in trouble if it filed returns for several years valuing inventory at cost, since market was higher than cost, and then wanted to use the valuation at market in a year when market dipped below cost. His thinking was that the Internal Revenue Service might well contend at this point that the original election of inventory valuation on the first return had been valuation at cost. Some years ago, corporate tax returns used to contain a line for indicating the method of valuing inventories. Since this has been dropped, it might be well for us to consider on the first return of new taxpayers indicating that the election was being made to value inventories at cost or market, whichever lower.

Use of More Taxable Entities

Leaving the matter of deferment of paying tax, and assuming a tax must be paid currently, our goal is to pay tax at the lowest possible rates. One significant area for discussion is having more taxable entities, together with having income taxed to the entities in the lowest tax brackets.

The benefits of more taxable entities are obvious—the more pieces the income pie is cut into, the lower the over-all average tax rate. To secure more taxable entities, we think of multiple corporations, division of income with members of families, trusts, etc.

Estates

Consider estates in the process of administration. It is generally desirable to keep an estate "open" as long as possible, from an income tax viewpoint, so that it will furnish another taxable entity for division of income. This is not universally true, as there may be situations in which the estate has a sizeable income and there are several residuary legatees, all in low tax brackets, who will divide the income when administration of the estate is completed. In the more usual situation, however, of total family income being divided to some extent between the estate and either a surviving spouse or a surviving child, prolonging the administration of the estate is generally a desirable tax objective. Of course, an estate cannot be kept "open" indefinitely merely to save taxes—there must be some valid reason. Often awaiting audit of Federal estate and State inheritance tax returns is a good reason.

One interesting possibility of keeping estates "open" arises from section 6166 of the Internal Revenue Code, providing for installment payments of estate tax over a period of ten years if the estate meets certain qualifications. There are good indications that the estate may be "kept open" for ten years as an income tax-paying entity, in order to have it alive to make these installment payments. It may be difficult to qualify under section 6166 and comply with the rather involved requirements as to acceleration of payments of estate tax under certain circumstances. The income tax savings, however, can well warrant the bother of qualifying and continuing to qualify for installment payments. Assume, for example, that an estate and surviving widow have combined income subject to tax of $40,000, which is equally divided between them during the period of administration, but will all belong to the widow when the estate is closed. As long as the estate is in process of administration and is a taxpayer, the combined tax under present rates would be $14,520. When all of the income becomes taxable to the widow, her individual tax would be $20,154. Certainly the saving of over $5,600 a year is worth a little paper work!

Multiple corporations

The use of multiple corporations has been an attractive method of lowering the over-all corporate tax rate. Organizing with a number of corporate entities, instead of only one, can result in a saving of up to $5,500 a year for each additional corporation due to its surtax exemption. In addition, each corporation is entitled under the 1958 amendments to the Internal Revenue Code to a minimum accumulated earnings credit of $100,000, which may be reassuring if there are uncertainties as to whether it can be satisfactorily proved that all funds are utilized in the business. It is important to consider *at the time of incorporation* whether multiple corporations might be useful at any time in the future—once assets have been placed in one corporation, it may be difficult, or impossible, to transfer some of the assets to new corporations and secure any additional surtax exemptions or minimum accumulated earnings credits.

In organizing into multiple corporations, it is well to follow some logical division, such as geographical areas, separate retail locations, separate functions such as manufacturing, selling, etc. The recent

Minnesota District Court case of James Realty Company, 59-2 USTC para. 9660, decided September 1, 1959, is quite disturbing to multiple corporation cases. In this case, the government was upheld in disallowing a corporation's surtax exemption, on the ground that there was no business purpose for the creation of the taxpayer corporation. This corporation was one of about a dozen organized by an individual to conduct his real estate development business. The operations among the related companies were of a type quite common in the real estate business. If this decision is upheld at higher levels, it can well mean difficulty to many multiple corporate organizations, particularly if the added corporations are mere bookkeeping entities, with no differences in management, transactions, etc.

Another even more recent case is Aldon Homes, Inc., 33 TC No. 65, decided December 29, 1959. In this case, involving a project for the construction and sale of 237 homes in the Los Angeles area, sixteen "alphabet corporations" (so-called because the name of each started with a new letter of the alphabet) were held not formed for substantial business purposes or to have engaged in substantial business activities. All income was therefore taxed to Aldon Homes, Inc., which actually controlled the project. Damaging facts were that the "alphabet corporations" had no employees, that the same employees in the same office kept the books for all seventeen corporations, and that Aldon Homes, Inc. and its stockholders did not deal at arms length with the "alphabet corporations."

The IRS has been very active in the multiple corporation field in Southern California, particularly in regard to real estate ventures. I have heard that there are 1,500 multiple corporation cases pending in that area alone. Aldon Homes is by no means the most extreme case—one involves *332* corporations, with a series of corporations named after flowers and another series after fish! We can hope that these extreme cases are examples of "hard facts making hard law"—we should still exercise considerable caution in the use of multiple corporations in view of the recent trends.

Subchapter S Corporations

One particular statutory method of paying lower tax rates, introduced by the 1958 amendments to the Internal Revenue Code, is the use of the Subchapter S corporation. This election gives the businessman the opportunity to choose between three methods of paying tax on his business income. He can:

1. Pay individual tax rates, under a proprietorship or partnership.
2. Incorporate his business and pay regular corporate tax rates.
3. Have his business incorporated, but pay individual tax rates on the net income by making the Subchapter S election. He will still have any advantages of the corporate organization, such as "fringe benefits" for officer-stockholders, who would not be entitled to these as partners or proprietors.

The Subchapter S election, however, should not be made lightly, as it cannot be changed from year to year. Once an election has been made to be taxed under Subchapter S, this must be continued until the election is voluntarily revoked or involuntarily terminated. Once an election has been revoked or terminated, a new election cannot be made for five years, unless permission is secured from the Commissioner of Internal Revenue.

Requirements for qualification

Let us review briefly the requirements to qualify a corporation for the Subchapter S election. It must be a Simple, Closely-held, American, Business corporation. Keep in mind the word SCAB, and see below what each letter stands for:

S — Simple
  Not member of affiliated group
  Shareholders individuals or estates—no nonresident aliens
  Not more than one class of stock

C — Closely-held
  Not more than ten stockholders

A — American
  Domestic corporation—not more than 80 per cent of gross receipts from sources outside the U.S.

B — Business
  Not more than 20 per cent of gross receipts from investments

Interest in election

Keith Engel, our Washington tax partner, ascertained for me that there were approximately 60,000 Subchapter S elections filed up to February 1, 1959. Considering that there are something like 700,000 corporations in the country, and considering the thousands and thousands that obviously do not qualify for the election or to whom it would have no interest, it is apparent that a large portion of the possible corporations have made this election.

Possible benefits

What are these electing corporations trying to achieve—what are they striving for? We might list some of the possible benefits, and then discuss each briefly.

1. Stockholders in lower tax brackets than corporation
2. Use of corporate losses by stockholders
3. Corporation distributing or about to distribute a substantial part of its earnings as dividends
4. "Unlocking" a large capital gain
5. Deferral of tax by use of fiscal year
6. Shifting income by a transfer of stock
7. Fringe benefits for partners and proprietors

Stockholders in lower tax brackets than corporation

There are probably thousands of incorporated drug stores, insurance agencies, gas stations, etc. around the country with stockholders in lower individual tax brackets than the minimum 30 per cent corporate tax. Many of these small corporations are paying corporate tax on a few thousand dollars of net income each year, and the remaining corporate earnings after taxes are then "locked up" and probably unavailable to the individual stockholders without a second tax. It would be advantageous for such a corporation to make a Subchapter S election, and thus have the net income of the business taxed directly to the individuals with only one tax.

Use of corporate losses by stockholders

In the past, there has been some reluctance to incorporate new business ventures. New businesses have a way of losing money until they become established, and owners have not wanted to depend solely on using such losses as carryovers against possible future corporate profits.

The Subchapter S election affords an opportunity for individual stockholders to get tax benefits from the corporate losses by taking them as individual deductions. This gives the individuals an opportunity to save tax *now,* instead of waiting for the benefits from corporate carryovers.

If the individual's share of corporate losses creates a net operating loss for the individual, it can be carried back only to 1958 and subsequent years. This means that the possibility of benefitting from the corporate losses will be improved until 1961, the first year in which individuals will be entitled to a full three-year carryback of losses resulting from a Subchapter S election. With a full three-year carryback, the opportunities will be multiplied to offset any losses against past high income years. It should be noted that one disadvantage of losses which put the individual stockholders into a carryback or carryover position is that they may well lose the benefit of their personal deductions and exemptions in carryback or carryover years.

Corporation distributing or about to distribute a substantial part of earnings as dividends

A corporation which is now distributing a substantial part of its earnings, or expects to make substantial distributions in the near future, can do nothing but gain by a Subchapter S election. This follows because such a corporation and its stockholders are experiencing the worst of the "double taxation" we hear so much about—first a corporate tax on the earnings, and then a second individual tax when the earnings after corporate taxes are distributed in the form of dividends.

If more than a certain percentage of corporate earnings are distributed as dividends, it will always be beneficial to make the Subchapter S election. This percentage will of course vary from corporation to corporation, because of the tax brackets of stockholders and other variables, but can be computed for any corporation.

It should be noted that we have referred to not only corporations presently distributing substantial dividends but those that are about to distribute substantial dividends. The Subchapter S election may be a solution to any unreasonable accumulation problems of a corporation. When a company reaches a point where it seems it must either distribute substantial dividends or face an unreasonable risk of the accumulated earnings surtax being imposed, the Subchapter S election may well be in order.

"Unlocking" large capital gain

The statutory treatment of capital gains "passes through" from the Subchapter S corporation to its stockholders. Thus, each stockholder is taxable on his proportionate share of any capital gain realized by the Subchapter S corporation. The capital gains taxed to the stockholders are net, after deduction of any capital losses, and are limited to the total net income of the corporation—stockholders cannot report a capital gain from the corporation and also deduct an ordinary loss. If a substantial corporate capital gain is in prospect, a Subchapter S election may well be desirable to insure that the stockholders will be taxed on this large capital gain with only the individual capital gains tax. If the capital gain is received by a nonelecting corporation, there will be a corporate capital gains tax and then presumably a second individual tax when the capital gain, after taxes, is taken out of the corporation by the stockholders.

Until Subchapter S came along, a corporation expecting a large capital gain had to either pay the corporate capital gains tax (and have the capital gain after taxes still "locked up" in the corporation) or consider liquidating the corporation, under section 337 or otherwise. Now a Subchapter S election will eliminate the necessity of the corporate liquidation, and has one distinct advantage over a liquidation. Under the Subchapter S election, the stockholders pay capital gains tax only on the capital gains actually received from outsiders. Under the section 337 or other liquidation, the stockholders must pay capital gains tax on all increment in the value of their stock in the corporation. This may include substantial accumulated earnings from past years, and unrealized increment in value of corporate assets.

It should be noted that H.R. 9003, introduced in Congress in 1959, but not enacted, would prevent the "pass through" of capital gains to stockholders of Subchapter S corporations, unless the corporation had been an electing corporation at least three years.

Deferral of tax by use of fiscal year

A stockholder's share of the undistributed income of a Subchapter S corporation is taxed to him in his year in which a corporate year ends. For example, if a Subchapter S corporation is on a January 31 fiscal year, a calendar year stockholder would report in his 1960 return his share of the undistributed corporate income for its year ended January 31, 1960.

This affords the same opportunity for deferral of payment of tax as that used extensively in the past by partnerships. The Treasury Department obviously does not like this situation any better than they did the deferral by the use of fiscal year partnerships. They substantially curtailed fiscal year partnerships by requiring new partnerships to choose a fiscal year the same as that of their principal partners, and refusing existing partnerships permission to change to fiscal years other than that of their principal partners, unless of course permission was secured in either case. H.R. 9003 would make the rules for Subchapter S corporation fiscal years substantially the same as those now in effect for partnerships. There may be an opportunity now to have a new corporation adopt a fiscal year which will result in some tax deferral opportunities, and a year that could not be adopted at a later time, if the proposed legislation becomes effective. There is already difficulty in changing the fiscal year of an electing corporation, under the regulations under section 442.

Shift income by transfer of stock

Since the undistributed income of a Subchapter S corporation is taxed pro rata to its stockholders on the last day of its taxable year, there are opportunities for shifting income from high bracket taxpayers to low bracket family members by gifts or other transfers of stock near the end of the corporate year. This is even better than the family partnership, where it is generally impossible to retroactively transfer income, the best that can be expected being the shifting of income to be earned in the future. It is also simpler than gifts of stock in an ordinary corporation—any shifting of income would require payment of dividends, resulting in double taxation and perhaps other undesirable features. This is another example of taxing income to the most advantageous entity, previously discussed.

Fringe benefits for partners and proprietors

In recent years, it has become more and more desirable taxwise to be an employee and less to be an entrepreneur. The Subchapter S election affords an opportunity to "have your cake and eat it too" in this area. Officer-stockholders can pay individual tax on their share of the corporate earnings, as they would as partners or proprietors, and yet be corporate employees to secure tax-free or tax-protected fringe benefits. The value of retirement plans, sick pay exclusions, accident and health insurance, plans for payment of medical expenses, group insurance, continuation of officers' salary, and other fringe benefits may add up to a sizeable package.

Here again, beware of H.R. 9003! This proposed legislation would make these fringe benefits unavailable to principal stockholders of the Subchapter S corporation, by providing that they are not considered as employees.

Possible disadvantages and problems

We should not leave Subchapter S thinking it is all good. There are disadvantages and problems—a few of them which are discussed below are as follows:

1. Inapplicability to "growth companies"
2. Problems in distributions
3. Consents by executors of estates
4. Special classes of income
5. Sales of stock
6. Restriction on use of trusts for estate planning
7. Some disadvantages in comparison with a partnership

Growth companies

Growth companies are generally organized as corporations because this is the best structure, both from a business and tax viewpoint. They generally want to plow back their earnings, their stockholders are often in high individual tax brackets, and their growth is generally most rapid by plowing back earnings after corporate taxes into expansion of the business. There may, however, be special situations of losses or capital gains where a Subchapter S election may be advisable even for these companies.

Problems in distributions

There are so many pitfalls in distributing earnings of a Subchapter S corporation that this could well be the entire subject of another paper. We can say here only that in general it is best to distribute earnings as currently as possible (preferably within the same corporate taxable year as the earnings were received), and avoid the traps one may encounter if the election is terminated or there are other changes.

Consents by executors of estates

In order for a Subchapter S election to continue, new stockholders must consent to the election within thirty days after becoming stockholders. An estate is considered a new stockholder, and the executor or administrator must consent within thirty days after qualification.

It may be well for an individual stockholder of a Subchapter S corporation to authorize his executor in his will to execute a consent to continue the Subchapter S election. Otherwise, an executor, particularly a corporate fiduciary, may be reluctant to consent. Particularly is this true if the time for filing the consent is late in the corporate year, and by consenting the executor would subject the estate to tax on a substantial amount of corporate income, unless he could get assurance of cash from the corporation to pay the resulting income tax.

Special classes of income

The Subchapter S election loses much of its advantage when one is considering types of income not subject to the full corporate tax. Due to the dividends received credit to corporations, ordinary dividends are taxed to corporations at either 4.5 per cent or 7.8 per cent, instead of the usual 30 and 52 per cent rates. This difference may be significant when comparing the tax to be paid by an ordinary corporation with that to be paid by an electing corporation, whose stockholders would pay their full individual rates on their shares of any dividends received by the corporation. It may be particularly undesirable to elect where there are conditions of operating losses and dividend income.

Sales of stock

In any sale of stock of an electing corporation, careful analysis is required by both the buyer and seller and their representatives. It should be noted first that the "previously taxed income" is personal as to each stockholder, and is not transferable. Therefore the purchaser of stock of an electing corporation will secure no benefit from the fact that the person from whom he bought the stock might be entitled to receive substantial distributions from the corporation on a tax-free basis.

Other problems arise in connection with earnings or losses of the current year. Since the holder of stock on the last day of the corporate year pays individual income tax on his pro rata share of the entire year's earnings, a purchaser may well get in a situation of paying for corporate earnings up to the date of the purchase of the stock, and then paying income tax on these same earnings a short time thereafter. On the other hand, losses are allocated in proportion to the time stock is held by each owner, where ownership changes during the year, *but* the loss allocated is the loss of the corporation for the whole year—no consideration is given to what the amount of the loss, if any, might have been as of the date of sale of the stock. Inequities may well arise, therefore, since a seller may secure the tax benefits of a portion of a loss arising after he sold his stock, and contrariwise, a seller might be harmed if the corporate loss up to date of sale was computed and taken into account in fixing the selling price, and then the loss was substantially reduced by the end of the corporate year.

Restriction on use of trusts for estate planning

Since trusts cannot be stockholders of electing corporations, problems arise if individual stockholders of electing corporations attempt to set up trusts in their wills. Also, of course, individuals cannot make gifts of stock of an electing corporation to trusts during their lifetime. The result is a limitation on the use of what may otherwise be a very desirable estate planning technique.

Disadvantages in comparison with partnership

Electing corporations have often been likened to partnerships. In comparison with partnerships, however, electing corporations have some disadvantages, two of which are as follows:

1. On any tax-free contribution of appreciated property to an electing corporation by a stockholder, the other stockholders are "stuck" with a low corporate tax basis for the property, with no opportunity for any election such as may be made by partnerships.
2. There is no new tax basis for corporate *assets* on the death of any stockholder of an electing corporation, as there would be on the death of a partner. A new, and presumably "stepped up" tax basis, applies only to the *stock* of the electing corporation. The corporation is still a separate taxable entity, and its tax basis for its assets is unchanged.

Conclusion

When one entity is expected to have a large amount of ordinary income in one year, progressive rates create tax problems. To solve these problems, tax deferral possibilities should be utilized to the maximum—then consideration should be given to dividing the income with other entities, by utilizing trusts, multiple corporations, or having income taxed to low-income members of the family. The Subchapter S election offers a special statutory method of having income taxed to the most advantageous entities.

We should keep in mind that any reductions of taxes we help our clients accomplish by planning save "100-cent dollars"—any costs of the planning are deductible, so are paid with "9-cent" to "80-cent" dollars, depending on tax brackets.

Durwood L. Alkire
Seattle

Durwood L. Alkire has a B.A. from the University of Washington and is a partner in our Seattle Office. He is active on committees of the Seattle Chamber of Commerce, the Municipal League of Seattle and King County, and the United Good Neighbor Fund.

What Are "Ordinary and

Reviewed by John S. Crawford, Portland

ONE OF THE RESULTS of high income tax rates has been the importance placed upon the deductibility of expenditures made by individuals as well as by business entities. Ordinary and necessary expenses meet the tests of deductibility. The problem faced by tax practitioners and businessmen is that of distinguishing expenditures which qualify as ordinary and necessary from those which do not. The theme of the subject book is to differentiate for the reader the expenditures which qualify from those which do not and to point up ways of assuring that proper deductions are not lost by careless record keeping or lack of proof. The authors commence with the general rule that Congress intended the income tax laws to tax earnings and

African safari—is this an ordinary and necessary business expense for an American dairy? Authors William Carson (left) and Herbert Weiner give their answer in a new book reviewed below for Quarterly readers.

Ordinary and Necessary Expenses

by William K. Carson, CPA and Herbert Weiner, CPA

The Ronald Press Company, New York, 250 pages

ecessary" Business Expenses?

profits less expenses and losses and proceed to such refinements as the deductibility of a safari in Africa by officers of an American dairy.

The authors state that the purpose of the book is to "present a practical approach to the problem for corporate executives, investors, professional taxmen, and for the many others engaged in all phases of business and professional endeavor who must assume responsibility for the recognition and solution of tax questions." They go on to do an excellent job of phrasing technical problems and rules in language that the average businessman or accountant can understand and use numerous examples to point up the controversial areas.

Chapter one presents the problem in general. First, the authors point out that there must be authority for the deductibility of the expenditure. The Internal Revenue Code of 1954 provides the statutory authority at sections 162(a) and 212 for ordinary and necessary expenses not specifically covered in other sections. From the deductible items they move to the nondeductible areas of personal expense, items to be capitalized, those against public policy and those specifically nondeductible by statute.

The five major test areas of any item claimed as a deduction are:

1. Is it a personal expense or does it otherwise fail to meet the "business" requirements of the code?
2. Is it an extraordinary expenditure required to be capitalized?
3. Does it violate public policy?
4. Is it disallowed by one of the statutory provisions designed to prevent unintended benefits?
5. Is it allowable, if at all, under another category of deductions or is it includable in cost of sales?

If the answer to all of the above questions is "no," the item is deductible as an ordinary and necessary expense. After discussing the above test areas generally for some twenty-four pages, the authors apply these tests to specific areas.

Moving from the formal areas of deductibility and nondeductibility, the book discusses the problem of determining whether the form of the transaction reflects its substance. A salary in form may be a dividend in substance. If so, what is deductible in form will be nondeductible in substance and substance controls.

The book is particularly valuable in respect to its discussion of such intangible subjects as public policy and unintended benefits. While the public press in full of comments on the abuses by businessmen and other taxpayers of travel, entertainment, club and promotion expenses, this book is one of the few places where a cool and impartial analysis of the problem areas can be found.

Going from the general areas of introduction, the book moves to a discussion of the application of the five tests to specific problems, in alphabetical order, for 110 pages. From advertising expenses it goes to compensation for personal services and from there to club dues. The most interesting, as well as the most authoritative, cases are discussed. Educational expenses and employees' benefits, as well as expenses of employees, are covered. Farmers' expenses, fines and penalties, hedging losses and expenses of illegal businesses are discussed. These are only a few examples of the business expenditures to which the five tests have been applied.

It is here that the auditor can see examples of the situations he should be looking for in examining the records of a business. From these examples he can get a feel of whether or not the client is treading on thin ice from a tax viewpoint with certain of its expense policies.

The full time tax man and the person who prepares an occasional return will find the cases cited a valuable aid in locating the complete reasoning of the courts on the particular problems. By using these cited cases as a starting point, other cases as well as rulings in the problem area can be located in the major tax services.

The authors then provide fifty pages of cases on ordinary and necessary expenses. They give a brief statement of the facts and a brief statement of the Court's holding and the reasoning upon which the holding was based.

Most accountants will receive the greatest value from the general discussions and the factual case examples given. On the other hand, persons specializing in tax work and who are familiar with the general principles will find at least two valuable aids. The first, in the form of annotations, has been referred to before. The second area is the benefit of the editorial comments of two experts who have made a concentrated study in a relatively restricted field of income taxation. The authors have made an intensive study of all ordinary and necessary expenses and are in a position to determine if a particular decision on a particular deduction is unduly restrictive or misleadingly broad.

In closing, the authors take thirty-two pages to advise the steps to be taken to obtain the greatest possible tax benefit from expenditures and to avoid the claiming of improper deductions or the disallowance of proper deductions which cannot be proven.

Each of the sections referred to above makes an interesting and valuable evening's reading. A tax man will be a better tax man after reading it and, perhaps just as important, an auditor will be a better auditor. Both will be in a better position to discuss a client's problems with him and to advise him of better ways to protect the deductions to which he is entitled and of helping him to avoid controversy in areas where expenditures are nondeductible.

Each member of Touche, Ross, Bailey & Smart could probably avoid overlooking deductions in the preparation of his own return by spending a few hours in reading sections of this book.

Clients attend seminar on Linear Programming

CLIENT personnel and TRB&S people from various offices joined the Management Sciences Division at a Linear Programming Seminar given November 18-20 in Detroit. The seminar was organized by Dr. George O'Brien who, together with Dr. Ernest Koenigsberg, gave an introductory session on the first day.

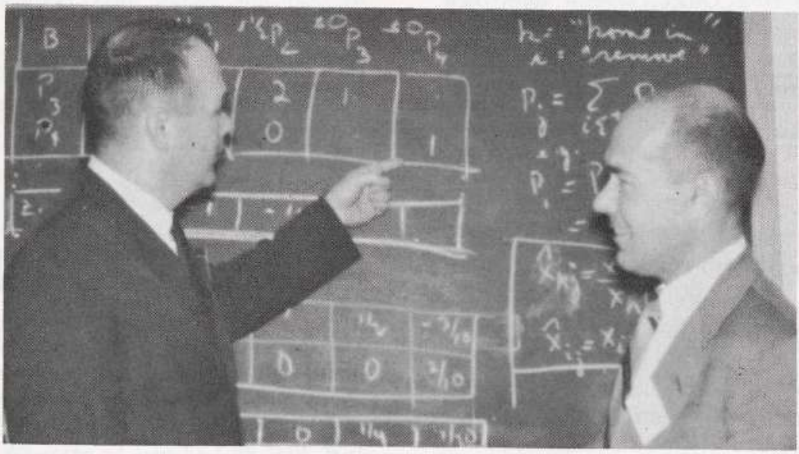
Guest speakers at the seminar were Dr. Abraham Charnes, Research Professor of Applied Mathematics and Economics at Northwestern University, and William W. Cooper, Professor of Economics and Industrial Administration at Carnegie Institute of Technology. The two men are the leading experts on linear programming in this country.

The joint lectures given by Messrs. Charnes and Cooper covered the following topics:

1—Planning and assessing the assembly of data for decision making.
2—Handling large-scale problems.
3—Programming and capital budgeting.
4—Internal pricing, costing and delegation models.
5—Stochastic and chance constrained programming.
6—Constrained games and information measures.
7—Concluding observations.

On hand to hear the lectures were Peter Stroh and Philip Whelan, Stroh Brewing Company; Gomer Redmond, Dave Woellner, Howard Ambill, Dennis Price, Herbert Whitecraft, and Harry Raden of the Chrysler Corporation; William Hart of Hamm Brewing Company, James Grace of General Mills, Ralph Hodges of the Mead Corporation, William Mitchener of Parke Davis and Co., Jack Thornby of Pillsbury Company, and Tom Sparrow of the University of Michigan.

Professor Abraham Charnes spoke to interested audience of 50 people.



Professor Cooper (right) clears up a point for Howard Peterson.

From left, Paul Hamman, Wilfred McLaughlin, Stroh's Peter Stroh, Chrysler's Harry Raden and Wallace Jensen relax a bit.

We Present . . .

Our New Associates

Baltimore—Marjorie M. Patterson is the secretary at our newest office.

Boston—Due to rapid expansion in the Boston Office, several new men were added to the staff recently. They are David P. Harris, University of Rochester; Edward J. Harrington, Boston University; Richard A. Farrar, Boston University and New England College; Roger A. Gould, Boston University; James R. Collins, Boston College. Robert E. Wanders is working with the Boston Office on a temporary basis while continuing his education at the Bentley School of Accounting and Finance. Paul R. Fetterolf is interning with this office; he is from the University of Pennsylvania.

Dallas—Patrick L. Weekley and James F. Leeper, Jr. became Dallas Office staff men in October. Mr. Weekley graduated from Howard Payne College and has done graduate work at Texas A & M. Mr. Leeper graduated from Oklahoma University and also did his graduate work there. Later in February the Dallas Office welcomed Gus C. Tramp, a January graduate of the University of Texas, and James R. Daffron, a January graduate of Southern Methodist University. Mrs. Leona Lowry is the new office bookkeeper at Dallas.

Dayton—Douglas Strain, Alfred E. Fisher, Shelton Sweress and Rust Gray have joined the audit staff. Mr. Strain graduated from Ohio State University in 1956 and served three years as an Air Force navigator. Mr. Fisher goes back to OSU for the spring quarter to complete his undergraduate work. Messrs. Sweress and Gray are recent graduates of OSU and DePauw, respectively. Nancy L. Stauter is a new member of the typing staff.

Denver—Gerhart P. Japha, associated with Fox, Samelson & Company for many years, has been appointed manager in the Denver Office.

Detroit—Gerald A. Murawski, a student at Michigan State University, is spending his winter term as an intern on the Detroit audit staff.

Seven University of Detroit accounting students — Robert E. Damaske, Diane C. Kruzman, Joseph J. McSweeney, Eugene J. Mierzejewski, Henry P. Mitchell, Joseph W. Polec and Lawrence C. Puchelski—worked on the audit staff here during their Christmas vacation and between semesters.

Richard A. Patterson joined the audit staff on graduation from the University of Michigan in January. He has an MBA degree.

Lois Coates and Sandra Katz are recent additions to the Detroit typing department.

Houston—Donald E. Mitchell, University of Houston, joined the tax staff in December. J. Rolfe Johnson, a junior at Rice Institute, came on a part-time basis in January.

Kansas City—Virgil Brummer of Kansas State University and Jerry L. Spotts, University of Kansas, interned here during January. Marianne Squires is the new receptionist and switchboard operator. Mary Jo Lower and Norma White have returned to the typing department after leaves of three years and three months, respectively.

Los Angeles — John J. Balian, University of Southern California graduate, joins our tax staff. For the past three years he has been with the United States Treasury Department.

Daniel Kurily, University of California graduate, came to the audit staff recently. Thomas Gogo, University of Southern California graduate, joined this office on February 1.

Management Sciences — Six men joined the Management Sciences Division staff recently.

- Albert L. Arcus — University of Western Australia, Oxford University, University of California. His experience includes positions in business, industry and government in Canada, Australia, Japan, Indonesia and England.
- James R. Bragg, CPA—University of Pittsburgh, formerly worked for IBM as a sales representative.
- Richard K. Davis—Columbia University and University of California. Formerly employed by Remington Rand Univac Division.
- Charles E. Hancock, Jr.—General Motors Institute and University of Michigan. Formerly employed by the Blackmer Pump Company as assistant to the superintendent.
- William D. Power—University of Oklahoma. Formerly Manager of the Retail Marketing Department, Remington Rand.
- J. Donald Volante, New York University. Formerly employed by Kimball Manufacturing Company.

Milwaukee—The new man in the tax department, Robert A. Weninger, has his BBA and LLB degrees from the University of Wisconsin.

Minneapolis—New faces here include Mrs. Cherry Allen, who will be in charge of bookkeeping, and two University of Minnesota interns, Daryl Johnson and Dene Rachuy.

New York — Eleven new associates recently joined the New York staff.

- Michael P. DeBlasio — St. Francis College
- Roy M. Furmark—Pace College
- Arthur H. Heiman—University of Rochester and Columbia
- Peter L. Klausner — University of Pennsylvania
- Thomas I. Marcosson—Union College, New York University
- Stuart Newman — City College of New York
- Arthur J. Radin — Columbia and New York University
- Ted Reiss — Brooklyn Polytechnic Institute and New York University
- Gerald Rosenfeld — Brooklyn College
- Frederick Singer—City College of New York
- Robert W. White—Upsala College and Syracuse University

Interning for the season are Robert

J. Batsavage and Sheldon Liberman, University of Scranton; Patricia M. DiSario, Pace College; Melvin S. Holtzman, Rutgers University; William F. Lukaswitz, Cornell; Thomas R. Maschal, University of Maryland; Frank A. Scudieri, Adelphi College, and Joseph E. Shelley, St. Francis College.

Portland — Ronald Maynard is the new Multilith operator here.

St. Louis—Welcome to Raymond T. Gusnard, CPA, and Gerald J. Otten. Mr. Gusnard graduated from St. Louis University, Mr. Otten from the University of Missouri with a master's degree in accounting.

Seattle—This office greeted three new staff men in December—Richard S. Coberly of the University of Washington and two interns from Montana State University, John C. Bryant and Ralph M. O'Brien. In January, Richard E. Pedersen and Patrick J. Peyton, both students at the University of Washington, reported for part-time duty. Richard W. Farmer joined the Seattle staff in February as a transfer from Ross, Touche & Co. in Vancouver, with whom he had been associated for seven years.

Washington, D. C. — Mrs. Charlotte S. Myrick joined the Washington Office as bookkeeper. A graduate of the Strayer Junior College of Finance, Mrs. Myrick formerly worked for the Federal Bureau of Investigation.

More about TRB&S in Denver

The merger with the Denver firm of Fox, Samelson & Company, which became effective December 1, 1959, was announced in Denver on January 1, 1960. The announcement was timed to coincide with the change in firm name.

The Denver Office is unique in that it occupies a one-story building, located a short distance from the downtown area, designed by and built to the specifications of Fox, Samelson & Company several years ago. However, the expanded activities of this new office will probably necessitate a move to larger quarters well before the end of 1960.

New Denver Partner

Resident partner Arthur Samelson was born in Denver and attended the University of Denver. He joined the accounting staff of a firm of local practitioners in 1935 and became a partner in 1940. Later that firm became Fox, Samelson & Company. Mr. Samelson and his wife, Raleigh, have two daughters, Judy and Andra Jo.

TRB&S in Service

Chicago—Servicemen Glen Hartung and Stanley Holdeman, home for the Christmas holidays, took time to stop in and greet their many friends in the Chicago Office.

John True writes from Fort Meade, Maryland that he is now attached to the Signal Air Defense Engineering Agency, which does testing and handles the administration for future air defense systems.

Dayton — Jerry Wheeler left recently for a six-month tour of active duty.

New York — Don Shagrin, presently away on a six-month tour of duty, will return to New York April 25, immediately following his honeymoon.

Changes of Scene

Denver — Carleton H. Griffin transferred from the Detroit Office in December to assume his new duties as head of the tax department. Frank Masden of Kansas City, Egil Stigum of New York and Donald Sinsabaugh of Dayton transferred to the Denver Office to join the audit staff.

Detroit—Lyman B. Curtis, Grand Rapids tax supervisior, transferred to the Detroit tax staff, while Robert P. Fairman moved from the Detroit tax staff to the Grand Rapids Office.

Grand Rapids — Philip R. VandenBerge transferred to the Grand Rapids Office from Detroit in November.

Los Angeles—James R. Ashby transferred from audit to management services, while Floyd R. Parkin went from the audit staff to the tax department.

Management Sciences — Joseph F. Buchan, formerly assistant to the Management Services Committee, has transferred to the Division of Management Sciences where he will establish and be in charge of Technical Training and Communication. He expects to devote about half of his effort to national management services activities.

With The Alumni

Chicago — After five years with the tax department, John Kelley has resigned to devote his time to setting up his own law practice.

News has reached us of the success of two former Chicago staff men. William Anderson has now become treasurer of The Creamery Package Manufacturing Company, while Charles Beauregard is the new treasurer of Skil Corporation.

Dayton — Gene Roberts, formerly of the audit staff, resigned in December to accept the position of internal auditor for the Rike-Kumler Co., Dayton, a newly acquired division of Federated Department Stores, Inc.

Detroit—Jack K. Wirth, audit supervisor, left February 29 to accept an appointment on the staff of the treasurer of Continental Aviation and Engineering Corporation, an old and valued client of the Detroit Office.

Houston — David S. Pitts, supervisor on the Houston staff, left the firm on

With The Alumni —continued

January 31 to accept a position as secretary-treasurer of Dixie Carriers, Inc. in Houston.

Kansas City — William M. Smith, audit senior, left to take a position as controller of a Kansas City Office client, Midwestern Financial Corporation. Loren E. White, who left the audit staff to take a position with a client, has returned to TRB&S.

Milwaukee—Gerald I. Boyce of the tax department left in January to be an assistant to the president of Preway, Inc. in Wisconsin Rapids, Wisconsin.

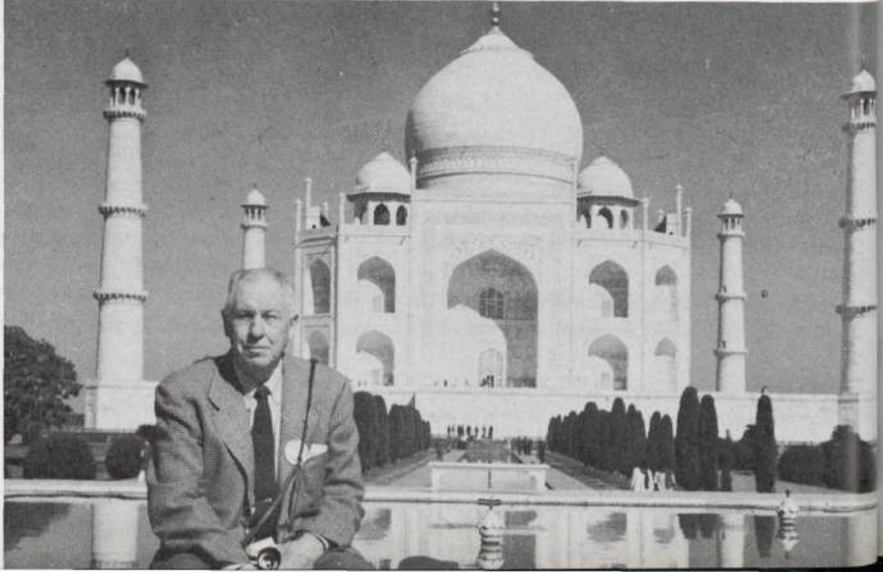
New York—Eugene P. Hagan was recently elected a vice president of Worthington Corporation. He will continue as controller, a post he has held since 1958.

Reporter Ellen Harden writes, "Congratulations are in order for Harry Dakin, who recently retired. The news just leaked out that he remarried this past summer—but he won't give us any of the details. Bill Nesbitt was in the office recently, too—he looked fine and is enjoying his leisure, doing all the things he always wanted to do. Latest project is rebuilding the percussion chamber of a player piano." Anthony Daly of New York wants to report a tip he received from Bill for the benefit of readers who may have yellow piano keys: Use No. ½ sandpaper, followed periodically by a mixture of whiting and alcohol.

Portland — Fifteen staff people gave Edward O. White and Bud Smith a farewell party at Edward H. Ericksen's home recently.

Advisory Partner George Ba

George Bailey recently returned from a trip to Africa, India, Malaya and other exotic places.



TRB&S in Action

Boston—As a result of two installations of Selective Inventory Management (SIM) now being made by the Boston Office, Donald Keller presided at a meeting on various aspects of this subject for the Boston staff. A review of Profitability Accounting was included, presented by Stanley Hart and Robert Hall who had attended the Profitability Accounting Seminar at the New York Office.

Chicago—Henry Korff, who has been serving as personnel manager of the Chicago Office, was recently made the administrative manager of that office.

Detroit—On December 1 the Detroit Office entertained the accounting faculty of Michigan State University at a dinner at the Detroit Athletic Club. Following dinner a review of experiences and problems was presented by various members of the faculty and our firm.

Houston — A staff meeting was held in the Houson Office on December 12 to discuss new tax matters and review office procedures and firm policies. The following staff personnel presented explanations and suggestions in connection with the subjects mentioned:

Herbert J. Brewer, manager—general firm policies and a list of suggested reading material for the staff.

Thomas C. Latter, manager — revision of tax guide for audit staff and suggestions of how he, as a reviewer, would like to have tax matters handled by audit people.

Leland C. Pickens, supervisor, Management Services—what management services has to offer and ways of bringing it to the attention of our clients.

Mrs. Burta Raborn, Tax Department—new Texas Franchise Tax explained.

Kansas City—The annual staff meeting was held December 24 with Mary McCann in charge. Discussions were led by Gary Doupnik, Forest De Haven, Loren White and Gale Hoffman.

Milwaukee — Robert Beyer attended an American Management Association Seminar on "Marginal Income Concept" in New York, January 25-27. Jack Schuett also attended an AMA seminar in New York on "Analyzing Operations for the Application of Electronic Data Processing."

Minneapolis—Two meetings covering insurance were held in the offices of a client, Charles W. Sexton Company. Discussions were led by Mr.

Active in Freedoms Foundation

FREEDOMS FOUNDATION is a nonpartisan organization of national scope which recognizes articulate contributions to the American way of life as distinguished from the increasing tendency toward authoritarianism. George Bailey is a long-time director.

At Valley Forge on February 22, Mr. Bailey presented an award to Secretary of the Army Wilbur Brucker. Mr. Bailey also presented secondary awards in the Detroit area. Both occasion received considerable publicity.

Other directors of the Foundation include Admiral Lewis Strauss, former chairman of the Atomic Energy Commission, and Colonel Willard Rockwell of Pittsburgh.

(continued on next page)

Hearle, president, and Mr. Hardell, executive vice president.

A series of staff meetings, presided over by partners and staff members, covered English, income tax return problems, profitability accounting and, for the last meeting, a series of brief presentations covering problems in the office and working in clients' offices.

The finale was a skit under the direction of Jim Flaa which burlesqued a typical audit. It opened in a client's office where the controller, James Ascher, and his girl bookkeeper, Delwyn E. Olson, patiently awaited the arrival of the auditors. The scenes following dramatized the blase behavior of the senior, William Oudal, and the tribulations of the junior, Jerry Sill, as he attempted to carry on during the next month catching errors that didn't exist, ferreting out a crook by comparing 1959 entries with a 1956 journal, etc.

San Francisco — "The cost program currently being promoted by the San Francisco Office for members of the Pacific States Cold Storage Warehousemen's Association in both Northern and Southern California has received impetus in the last several months from a series of conventions and seminars sponsored by us to instruct association members in our unified cost accounting system," San Francisco reports.

"The first meeting consisted of our participation in the Association's 37th annual convention held at Santa Barbara in October. Wayne Mayhew and Dale Bowen spoke on 'Cost Finding by Accounting Procedures,' which ended as a two-hour session. Then early in December the Northern California members of the association attended a cost accounting conference at the Sheraton-Palace Hotel in San Francisco which was handled entirely by our staff. Dale Bowen acted as chief instructor since the conference was intended as a form of seminar; he was assisted by Ben Druckerman, Richard Brown, Leo Feltz, and Malcolm James."

A second indoctrination and training seminar was held in the Los Angeles Office for the Southern California group on December 21-23. Dale Bowen and Jack Heil (Los Angeles) conducted this program, assisted by Ben Druckerman and Denis Crane of the San Francisco staff and James Ashby of the Los Angeles staff.

There are 10 cold storage companies with 17 plants in the northern group and 9 companies with 20 plants in the southern group.

A similar conference under the auspices of the Western Frozen Food Processors Association was held at San Jose in November for the benefit of frozen food processors. A general discussion primarily for operating managers and controllers opened the conference while the rest of the time was devoted to a training course in the application of our uniform system for their industry. Dale Bowen and Malcolm James represented TRB&S on the discussion panel, while Denis Crane conducted the training sessions.

Seattle—Sixteen staff members participated in the training session on January 2 which concerned working paper preparation, the mechanics of financial statement preparation, and office procedures. The session was conducted by Robert B. Hevly and Raymond F. Zoellick.

Congratulations to 40 new CPAs

Atlanta

Loretto G. Boswell
George C. Wright, Jr.

Boston

Donald M. Keller
Francis J. Mazzucotelli

Cleveland

Frank Brcak, Jr.

Dayton

E. A. Duff Macbeth

Denver

*Donald G. Sinsabaugh

Detroit

Henry E. Bodman, II
*C. James Clemens
*Marie E. Dubke
*John D. Hegarty, Jr.
Daniel J. Kelly
Roger C. Markhus
Gerald A. Polansky
Robert E. Shelton
David J. Vander Broek
*Richard T. Walsh

Grand Rapids

*Richard E. Herrinton

Los Angeles

Lawrence E. Baur, Jr.
Alex Borra
Irwin Leach

Milwaukee

*Benjamin L. Case
*Max Sporer
Peter E. Stolz, Jr.

New York

*Ronald Segel

Pittsburgh

*James P. Belack
*Theodore R. Miller

St. Louis

Eugene J. Schorb

San Francisco

Denis Crane
Edward Dewey
*Robert Faris
John Gale
Henry Maschal
James McComb
*Jerome Vernazza
Joseph Wood

Seattle

Stanley M. Bray
Guy C. Pinkerton
Harry G. Widener, Jr.
Raymond F. Zoellick

*Passed on first attempt.

NOTE: New York's David Hills and Edward A. Valenti, who were listed in the December Quarterly, also passed on the first attempt.

Applause . . .

Atlanta

Elwood R. Dryden addressed the Atlanta Chapter of the National Machine Accountants Association on November 19. His topic was "Public Accountants' Views on Electronic Data Processing." On January 20 he spoke before the Atlanta Chapter of the Institute of Internal Auditors on "Cooperation of Internal Auditors and CPAs during the Annual Audit."

William Tate, a member of the Taxation Committee of the Georgia Society of CPAs attended a Tax Forum on November 9-10 as representative of TRB&S.

Chicago

William J. Schwanbeck spoke before the Automotive Electric Association on December 6, discussing taxes and recent developments as to State Sales Taxes.

Allen C. Howard is now serving as the chairman of the Illinois Board of Examiners in Accountancy. He has also been elected to the Committee on Auditing Procedure of the American Institute of Certified Public Accountants (AICPA).

Kay H. Cowen participated in the 1959 Tax Conference of The Illinois Society of CPAs held in Chicago on December 3-4. He was largely responsible for a dramatization of the part the CPA plays in developing an estate plan for a client and was cast in the role of the tax man.

Cleveland

Carl A. Johnson addressed the Cleveland Controllers Group of the Controllers Congress on February 10. His subject was "Developments Affecting the Relationship Between the CPA and the Retailer."

Dallas

David Muir was panel moderator of a discussion forum on direct costing at the November meeting of the Dallas Chapter of the NAA. The forum was of major interest to local cost accountants as evidenced by the breaking of all attendance records at this meeting.

Dayton

Les Buenzow, a member of the Ohio Board of Accountancy, participated in a panel discussion at The American Accounting Association Ohio Regional Group Meeting. It was held at Ohio State University in Columbus on December 5, 1959. The topic of the discussion was "How the New Accountancy Law Will Affect Ohio Colleges."

Denver

Carleton H. Griffin wrote a tax article for the *Journal of Accountancy* entitled "Changes in Accounting Method" which appeared in the December 1959 issue. This article brought up to date one that had appeared in the

November 1958 issue of The Quarterly. Mr. Griffin was a co-speaker at a meeting of the Michigan Association of CPAs on December 14, his subject being "Problems of Closely Held Corporations."

Detroit

Donald R. Wood discussed "The Layman's Approach to Operations Research" before the Toledo Chapter of the Systems and Procedures Association on January 21.

Kenneth S. Reames was appointed to the State Legislation Committee of AICPA.

On January 21, Paul E. Hamman presented a discussion of Profitability Accounting to the Ann Arbor Chapter of the National Association of Accountants.

Donald J. Bevis has been reappointed to the Committee on Professional Ethics and the Committee on Responsibility for Clients' Acts of the AICPA.

On January 26 Wallace M. Jensen spoke at a meeting of the Atlanta Control of the Controllers Institute of America. His subject was "Current Developments in Federal Taxation." Mr. Jensen's participation in the meeting was arranged by Woody Dryden of the Atlanta Office.

Executive Office

Donald H. Cramer contributed a chapter on process cost systems to the second edition of the Accountants' Cost Handbook published by The Ronald Press.

Grand Rapids

Kenneth H. Nelson has been appointed director of education for the Grand Rapids Chapter of NAA.

Kansas City

Glen A. Olson attended the "Manufacturing Control" Seminar conducted by the Data Processing Division of the Kansas City IBM office.

Los Angeles

John S. Heil is a member of the Business and Industrial Consultants Committee of the Los Angeles Chamber of Commerce.

Milwaukee

Robert Beyer addressed the American Management Association (AMA) in New York on January 13. His subject was "Profitability Accounting." He also talked on the same subject to the Milwaukee Chapter of NAA on December 21.

Walter F. Renz addressed the Washington D. C. Chapter of NAA in Washington on November 18. His subject was "Profitability Accounting." On February 1 Mr. Renz addressed the Milwaukee Chapter of the Wisconsin Society of CPAs, speaking on "Management Services."

Donald Best talked to the Wisconsin Industrial Association at Manitowoc, Wisconsin on January 26. His subject —"Office Methods Improvements."

Lowell L. Robertson addressed the Beta Alpha Psi Chapter at the University of Iowa on February 11. He spoke on "Life in Public Accounting."

Wayne Mayhew, Jr. spoke to the Ohio Canners and Food Processors Association in Columbus on February 3. His subject: "Cost Accounting for Efficient Plant Operations."

Management Sciences

On November 1, Nicholas Radell

spoke to a Stanford University graduate seminar in retailing on "Inventory Management in Retailing." Also in November he addressed a meeting of the Operations Research Society of America in Pasadena on the topic, "Implied Costs as a Basis for Systems Design."

Dr. George O'Brien spoke on "The Use of Computers in Management Decision Making" to a meeting of the Eastern Joint Computer Association in Boston on December 3.

Roger Crane delivered a paper before an AMA seminar in New York on December 9. The title of this paper, co-authored with Alvin Wanthal, was "The Use of Scientific Techniques as Analytical Tools in the Acquisition Process."

Minneapolis

Clayton Ostlund was moderator for a panel discussion of "Independent Auditors' Responsibilities" at the December meeting of the Minnesota CPA Society.

Barton Burns spoke on the "Minnesota Income Tax Law Amendments" at the Annual Tax Conference for CPAs and Associates on November 20. Several staff members attended this conference and the conference held on November 19 for business executives.

Kenneth Schuba's article "Some Considerations in Arriving at Make or Buy Decisions" will be published in the March issue of the NAA Bulletin.

Barton Burns presented the speech "What Price Depreciation" at the regional convention of the American Poultry & Hatchery Federation held in Minneapolis in December. This speech was prepared by Gale Hoffman and was given in other cities at similar meetings.

James F. Pitt participated in a panel discussion sponsored by the Minneapolis Chamber of Commerce on the subject of taxation. It was taped and broadcast over radio station WLOL on February 14.

New York

William Bergen was reappointed for 1960 to the Character and Fitness Committee of the New Jersey State Board of Public Accountants.

William Carson has been appointed a member of the Estate Planning Council of New York City.

Joseph Levee spoke on "Current IRS Tax on Western Hemisphere Trade Corporation" before the New York State Society of CPAs Committee on Foreign Governments' Taxation on November 12.

Mr. Levee received very complimentary notes of appreciation from both the Executive Secretary and the Director of Research and Development of the American Poultry & Hatchery Federation for his address before a convention of that organization at the Hotel New Yorker on December 4. Parts of his talk are included with other material in the January issue of the *American Hatchery News*.

John Ehling, who is a panel member of the American Arbitration Association, served recently in that capacity.

Kenneth Mages gave a talk at the National Sales Meeting of Jantzen, Inc., in Atlantic City December 14.

January was a very busy month for Mr. Mages, as indicated below.

January 5—He received a Scroll of Appreciation from the Retail Re-

A. W. Hughes, left, chairman of J. C. Penny & Co., checks plaque given to Ken Mages by the National Retail Merchants Association.

search Institute of the NRMA for his participation in the establishment of the RRI.

January 11—He received a silver plaque at the National Retail Merchants Association convention "for his many contributions as consultant to the retail trade." Mr. Mages' photo and write-ups of the event appeared in STORES, the NRMA magazine; the *Department Store Economist,* and the *Women's Wear Daily.*

January 12—At this same convention he addressed the Credit Management Division on the subject of "Accounts Receivable Aging—The Public Accountant's Viewpoint."

January 20—He addressed a joint meeting of the Metropolitan Controllers Association and the New York State Society of CPAs on "Problem Areas Relating to Use of Electronic Equipment in Processing Department Store Accounts Receivable," at the Savoy Plaza Hotel, New York.

Pittsburgh

"Visiting Ford Distinguished Research Professor in the Graduate School of Industrial Administration" at Carnegie Tech is a long title which brings a great honor to Robert Trueblood. His appointment is for the period September 1, 1960 to May 21, 1961 and will require about 80% of his time, which will be devoted to research.

Richard P. McMurray was guest speaker at a dinner meeting of the Central Chapter, Pennsylvania Institute of CPAs, at the Penn-Alto Hotel in Altoona on November 24. His subject was "Management Services and the CPA."

Robert M. Trueblood attended a meeting of the Long Range Objectives Group of AICPA in New York, January 6-7.

On January 8 Mr. Trueblood attended a special meeting of AICPA Advisory Committee to its Tax Committee on the LIFO problem. This group, which includes Mr. Blough and Mr.

Broad in addition to Mr. Trueblood, is to develop a memorandum which deals with pooling the LIFO inventories through the use of the dollar value method, but considering the matter from an accounting viewpoint.

On November 10, Louis A. Werbaneth, Jr. delivered the principal address at the Beta Alpha Psi initiation banquet at West Virginia University.

Keith Engel of the Washington Office addressed the luncheon meeting of the Pittsburgh Chapter of the Pennsylvania Institute of CPAs on November 17. Approximately 90 people were there, including representatives of the larger clients in the Pittsburgh Office. During the afternoon, Mr. Engel was introduced to major officers of our larger clients and discussed their Washington problems.

Portland

John S. Crawford was moderator of the annual Tax Forum held in Portland in December. This forum was sponsored by the Oregon Society of CPAs and was attended by 450 accountants and attorneys from throughout the Northwest.

Harold Lemon was appointed to the Municipal Auditing Committee of the Oregon State Society of CPAs.

Edward H. Ericksen spoke before the Agricultural Cooperative Council of Oregon on December 7. His topic was "Indirect Expenses as Used for Decision Making."

San Francisco

On November 11 Dr. Ernest Koenigsberg lectured at Stanford University to the graduating class of the Graduate School of Industrial Engineering on "Operations Research in Coal Mining."

On December 7 Dr. Koenigsberg lectured at the Sloan Foundation class of the Graduate School of Business Administration at Stanford on "Status and Future of Management Sciences in Industry."

The San Francisco Chapter of the California Society of CPAs held an accounting systems conference on December 11 at the Mark Hopkins. Dale Bowen opened the meeting with a short introduction.

On November 19 Robert W. Johnson spoke before the meeting of the National Machine Accountants Association's East Bay Chapter in Oakland on "The System Designer's Responsibility to the Auditors in Installing Electronic Data Processing Systems."

Robert W. Johnson is now a member of the AICPA committee on statistical sampling.

On January 5-7 Paul Warnick attended the annual meeting of The National Council of Farmer Cooperatives in Atlanta. He is a member of the Accounting and Business Administration Committee.

St. Louis

Edwin H. Wagner, Jr. has been reappointed to the Advisory Committee on Professional Development of the AICPA.

On December 17 Mr. Wagner delivered a talk before the Oklahoma Society of CPAs in Oklahoma City. His topic was "Your Institute."

On December 30 James G. Carroll was a speaker at the annual meeting of the executives and buyers of Boyd-Richardson Company. He also attended the National Retail Merchants Association convention in New York.

Seattle

The Accountants Association of Olympia heard Dean D. Thornton speak on "Why the CPA" on January 20.

The next day Robert J. Mooney spoke before a meeting of the Pacific Mountain Chapter of the Associated General Contractors of America on the subject "Depreciation Applicable to the Heavy Construction Industry."

Washington

On January 12 Karney A. Brasfield was guest speaker at the Middle Management Institute sponsored by the United States Civil Service Commission. His topic was "Financial Data for Management Planning."

Mr. Brasfield will be chairman of the Financial Management Roundtable on February 23, when "Managerial Accounting—Is This the Answer?" will be discussed. The Roundtable is sponsored by the Washington Chapters of the Federal Government Accountants Association, the Society for the Advancement of Management and the American Society for Public Administration.

These Are Worth Reading . . .

The Elements of Style by William Strunk, Jr., with revisions by E. B. White, Macmillan, New York, 1959.

Less Risk in Inventory Estimates by Robert G. Brown, *Harvard Business Review*, July-August 1959.

Management's Role in Electronic Data Processing, Studies in Business Policy No. 92, National Industrial Conference Board.

After Hours . . .

Boston

Robert Hall has been registered as a candidate for election as Town Meeting Member in Braintree, Massachusetts. Stanley Hart has recently joined the local chapter of NOMA. Charles Noble has been appointed chairman of the Wesley Methodist Church Spring Fair to be held in Framingham, Massachussets in May.

Chicago

The annual dinner dance of the Chicago Office was held December 12 at the Union League Club. High point of the evening was the special recognition given Avis McKay, head of the Typing Department, for her 30 years of faithful service.

Dayton

John Bell has been elected Treasurer of the newly formed Miami Valley Chapter, The Institute of Management Sciences.

Dane Charles, a member of the Dayton Chapter CPAs' Junior Achievement Committee, participated in the preliminary review of JA companies made last January.

For the past several months Leon J. Sachleben has been active in the Citizens Advisory Council for cooperation with the local Board of Education. Mr. Sachleben has also taken over the duties of treasurer of Boy Scout Troop 110 of the Miamisburg Mound District.

Detroit

Robert D. Wishart has been elected to the Board of Deacons of the First Presbyterian Church of Dearborn for a three-year term. Mr. Wishart was also recently elected to the Board of Directors of the Dearborn Kiwanis Club.

H. James Gram was recently elected treasurer of the Grosse Pointe Memorial Church.

Executive Office

Henry Ford II, vice presidents John Cronin of General Motors and C. L. Jacobson of Chrysler plus many other notables were guests at a civic luncheon in January honoring two Detroit volunteer groups. Dolores DeWolf was chairman and Paul Hamman represented TRB&S at the speakers' table.

Mrs. DeWolf was a hostess at the unveiling of a portrait of the Honorable Mary V. Beck, president of Detroit's Common Council, on Feb. 29.

Houston

Shirley and Herbert Brewer have been elected secretary and treasurer of the Memorial Forest Civic Club for the calendar year 1960. Approximately 200 families belong.

Donald E. Mitchell has been active in Junior Chamber of Commerce

Ernest Koenigsberg's photo of daughter Johanna won newspaper prize.

work. He is currently serving as chairman of the Blood Bank.

On January 28 Owen Lipscomb accepted reappointment to the 1960 State and National Affairs Committee of the Houston Chamber of Commerce.

Minneapolis

The annual luncheon for staff and alumni was given in the Minneapolis Office on December 24, following the staff meeting. Several alumni from out of the state were present, as well as many local alumni who make frequent visits to our office as clients.

Mrs. James F. Pitt is the newly elected president of the Minneapolis Chapter of CPA Wives Club.

Pittsburgh

Robert M. Trueblood has been appointed to the Scholarship Committee of the Pittsburgh Chapter, University of Minnesota Alumni Association. Anthony E. Rapp has been elected assistant treasurer of the Pittsburgh Junior Chamber of Commerce.

St. Louis

Edwin H. Wagner was reelected treasurer of the Noonday Club for a fourth term. He was also reelected a director of Catholic Charities of St. Louis.

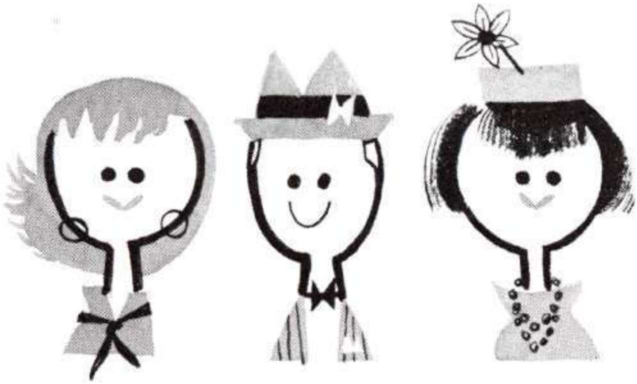
San Francisco

Ben Druckerman is running for city councilman of Mountain View. The election will be held in April.

Dr. Ernest Koenigsberg won a $10 prize for photography in a weekly contest sponsored by the *San Francisco Chronicle.*

Seattle

Edward P. Tremper has been elected a trustee and treasurer of the Seattle and King County Community Chest for the coming year. Gerald E. Gorans joined Mr. Tremper as a member of the Finance and Budget Committee of Century 21 Exposition, the 1962 Seattle World Fair. Mr. Gorans has also been appointed a member of the Citizens Committee for Evaluation of Vocational Education in King County.



TRB&S

At Home

Atlanta

Newcomers—Ronald Wade, November 13, to Mr. and Mrs. William A. Tate.

Boston

Newcomers—Wendy Joyce, December 11, to Mr. and Mrs. Philip Shapiro. Patricia Anne, January 21, to Mr. and Mrs. Charles H. Noble.

Chicago

Marriages—Frank Strachota to Joan Lichtenberger, November 21. John Brown to Joyce Quinnies, November 28.

Newcomers—David Madden, November 8, to Mr. and Mrs. Robert Shehan. Jacqueline, November 23, to Mr. and Mrs. John Van Camp. Linda Jean, January 7, to Mr. and Mrs. Raymond Perry. Linda Marie, January 9, to Mr. and Mrs. John Linster.

Dayton

Marriages—Dane W. Charles to Judy Coleman, November 18. E. James Dickerson to Roberta Kaser, January 30.

Newcomer—Annette Marie, November 2, to Mr. and Mrs. Francis J. Schubert.

Detroit

Newcomers—Edward Allen, November 10, to Mr. and Mrs. Thomas E. Drenten. Julee Lynn, November 27, to Mr. and Mrs. Merlyn K. Johnson. John Edward, December 8, to Mr. and Mrs. David V. Burchfield. David Robert, December 11, to Mr. and Mrs. Robert G. Stevens. Lynda Carol, February 18, to Mr. and Mrs. James H. Dunbar.

Executive Office

Marriage—Judith Staelens to Remy J. Van Ophem, January 9.

Grand Rapids

Newcomers—Craig Thomas, November 5, to Mr. and Mrs. Kenneth H. Nelson. Bruce Alan, January 13, to Mr. and Mrs. William Dahlquist.

Houston

Newcomer—Kim Suzanne, January 21, to Mr. and Mrs. Richard M. Pollard.

Kansas City

Newcomers—Michael, December 15, to Mr. and Mrs. Loren E. White, Karen Elizabeth, January 1, to Lt. and Mrs. Robert E. Plain.

Management Sciences

Newcomer — Katherine Sophia, February 13, to Mr. and Mrs. James S. Reiss.

Milwaukee

Marriage—Richard Valley to Marlene Pilut, December 26.

Newcomers—Steven Peter, November 10, to Mr. and Mrs. Peter Stolz. Suellen, December 22, to Mr. and Mrs. Paul Pakalski.

Minneapolis

Marriage — Jean M. Hagglund to Robert Dana Parshall, November 28.

Newcomer—Michael Allan, December 24, to Mr. and Mrs. Robert McWain.

New York

Marriage—Avron Brog to Sheila Liebler, November 26.

Newcomers—Jean, August 14, to Mr. and Mrs. James M. Lynch. Robert D. August 27, to Mr. and Mrs. Irving Allen. Donald James, September 3, to Mr. and Mrs. Donald J. Surdoval. Anna Roslyn, September 20, to Mr. and Mrs. Samuel Siegel. Matthew Bruce, October 1, to Mr. and Mrs. David Hills. Paul Charles, October 2, to Mr. and Mrs. Harry F. Brensinger III. James Robert, October 19, to Mr. and Mrs. John C. Emmert. Craig Stephen, December 25, to Mr. and Mrs. Stephen Lipka. Carl Oswald, January 5, to Mr. and Mrs. Oswald C. Wuestehube. Jill Wendy, January 7, to Mr. and Mrs. Leonard S. Schwartz. Bryan James, February 17, to Mr. and Mrs. Robert W. White.

Philadelphia

Newcomer—Margaret Anne, December 8, to Mr. and Mrs. William J. Byrne.

Pittsburgh

Newcomer—Bruce Alan, November 27, to Mr. and Mrs. Gary Fink.

San Francisco

Marriage—George Young to Barbara

Newcomers—Robert Jr., November 19, to Mr. and Mrs. Robert Estes. Richard, adopted November 27 by Mr. and Mrs. Richard Brown. Deborah Helen, December 21, to Mr. and Mrs. Peter Pors. Nancy Lynn, January 28, to Mr. and Mrs. Robert Faris.

Seattle

Newcomers—Mary Ann, December 14, to Mr. and Mrs. Richard C. Bennett. Kimberlee Paige, January 17, to Mr. and Mrs. Walter T. Porter, Jr.

QUARTERLY CORRESPONDENTS

MARIAN LANGLEY	*Atlanta*
MARJORIE M. PATTERSON	*Baltimore*
MARJORIE J. JOHNSON	*Boston*
SHERLE SWANSON	*Chicago*
ANNE MATYA	*Cleveland*
JOHN E. STEPHENSON	*Dallas*
SAM CHRISTY	*Dayton*
BEVERLY THOMAS	*Denver*
HARRY TROXELL	*Detroit*
PATRICIA HUBER	*Grand Rapids*
JEANIE LANNOM	*Houston*
GENEVIEVE SILADY	*Kansas City*
EVELYN MATTSON	*Los Angeles*
G. P. ALLEN	*Management Sciences*
BETTY TOMEK	*Milwaukee*
ALICE CARLSON	*Minneapolis*
ELLEN HARDEN	*New York*
ELIZABETH KEENAN	*Philadelphia*
MILDRED H. LONCOSKY	*Pittsburgh*
DAVISON CASTLES	*Portland (Ore.)*
MARY SHARKEY	*Rochester (N.Y.)*
DOROTHEA M. KRAMER	*St. Louis*
HENRIETTA BARTON	*San Francisco*
HELEN B. LILLY	*Seattle*
CORLAN JOHNSON	*Washington, D. C.*